650

Social Security

Budget function 650 comprises spending for the Old-Age, Survivors, and Disability Insurance programs, commonly known as Social Security. Social Security consists of two parts, each tied to a trust fund. The Old-Age and Survivors Insurance (OASI) program provides monthly benefits to eligible retired workers and their families and survivors. The Disability Insurance (DI) program provides monthly benefits to eligible disabled workers and their families. CBO estimates that Social Security outlays will total $433.1 billion in 2001. That amount includes discretionary outlays of $3.4 billion, which are for the administrative expenses of operating the Social Security program.

Federal Spending, Fiscal Years 1990-2001 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	Estimate 2001
Budget Authority (Discretionary)	2.2	2.4	2.5	2.6	2.8	2.3	3.1	3.5	3.2	3.2	3.2	3.4
Outlays												
Discretionary	2.1	2.3	2.4	2.6	2.7	2.6	2.6	3.0	3.1	3.1	3.4	3.4
Mandatory	246.5	266.8	285.2	302.0	316.9	333.3	347.1	362.3	376.1	387.0	406.0	429.7
Total	248.6	269.0	287.6	304.6	319.6	335.8	349.7	365.3	379.2	390.0	409.4	433.1
Memorandum:												
Annual Percentage Change in Discretionary Outlays		5.8	7.4	7.6	2.0	-2.9	2.0	12.8	4.9	-1.8	12.0	-0.8

650-01 Accelerate the Increase in the Retirement Age for Social Security Benefits

	Outlay Savings (Millions of dollars)
2002	0
2003	0
2004	0
2005	0
2006	50
2002-2006	50
2002-2011	9,350

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

650-02 and 650-03

RELATED CBO PUBLICATION:

Long-Term Budgetary Pressures and Policy Options (Report), May 1998, Chapter 3.

Under current law, workers born before 1938 become eligible for full Social Security retirement benefits at age 65. The normal retirement age (NRA) increases in two-month increments for workers thereafter, reaching 66 for workers born in 1943. It remains at 66 for workers born from 1944 through 1954. It then begins to rise again, also in two-month increments, reaching 67 for workers born in 1960 or later. Workers will still be able to start collecting reduced benefits at age 62. As the NRA increases, however, the size of that reduction will grow as the period between age 62 and the age at which a new beneficiary becomes eligible for unreduced benefits lengthens.

Members of Congress and others have recommended that the change to an NRA of 67 be accelerated. One option would steadily increase the NRA by two months per year until it reached age 67 for workers born in 1949. Under that option, the first cohort to have a normal retirement age of 67 would become eligible for reduced benefits (at age 62) in 2011, which is 11 years sooner than under current law.

The savings from that option would begin as workers in the first affected cohort (workers born in 1944) reached age 62 in 2006, and they would increase thereafter. Workers in that cohort who began collecting benefits at age 62 would receive about 1 percent less than they would under current law (about 74 percent of their full benefit, rather than 75 percent). The NRA for workers who reached age 62 in 2011 would be 67 rather than 66; they would receive about 7 percent less than they would under current law (70 percent of their full benefit, rather than 75 percent).

Because the first Social Security beneficiaries affected would not become eligible for benefits until 2006, federal outlays would be unaffected until then. Each year thereafter, the savings would grow as more beneficiaries were affected, with each successive cohort incurring larger reductions in benefits. Savings over the 2002-2011 period would total $9.4 billion. Because some Social Security beneficiaries with low income would qualify for federal means-tested benefits, such as Supplemental Security Income and food stamps, some of the savings in Social Security benefits might be offset by additional outlays for other programs. (That increase in outlays is not reflected in the estimates.)

Proponents of raising the normal retirement age point out that people age 65 today live several years longer, on average, than was the case in the early days of the Social Security system, that life expectancy is projected to continue to increase, and that this otherwise favorable development will raise the cost of the program. Opponents argue that raising the NRA is, for the most part, simply a means of cutting future monthly Social Security benefits.

650-02 Lengthen the Computation Period for Social Security Benefits by Three Years

	Outlay Savings (Millions of dollars)
2002	50
2003	150
2004	450
2005	900
2006	1,450
2002-2006	3,000
2002-2011	22,100

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

650-01 and 650-03

RELATED CBO PUBLICATION:

Long-Term Budgetary Pressures and Policy Options (Report), May 1998, Chapter 3.

Social Security retirement benefits are based on the average indexed monthly earnings (AIME) of workers in jobs covered by the system. The present formula computes AIME based on workers' 35 highest-earning years of employment. Lengthening the averaging period would generally lower benefits slightly by requiring more years of lower earnings to be factored into the benefit computation. This option would increase the AIME computation period gradually until it reached 38 years for people turning 62 in 2004 or beyond. That approach would save $3 billion over the next five years and more in later years. Because some Social Security beneficiaries with low income would qualify for federal means-tested benefits, such as Supplemental Security Income and food stamps, some of the savings in Social Security benefits might be offset by additional outlays for other programs. (That increase in outlays is not reflected in the estimates.)

One argument for a longer computation period is that people are now living longer and that lengthening the computation period would encourage people to remain in the labor force longer as well. In addition, lengthening the averaging period would reduce the advantage that some workers who postpone entering the labor force have over those who get jobs at younger ages. Because many years of low or no earnings can be ignored in calculating AIME, the former group currently experiences little or no loss of benefits for its additional years spent not working and thus not paying Social Security taxes.

Opponents argue that because some beneficiaries elect early retirement for reasons such as poor health or unemployment, this proposal would adversely affect recipients who were least able to continue working. Other workers who would be disproportionately affected include those with significant time spent outside the Social Security system, such as parents—usually women—who interrupted their career to rear children, and workers who were unemployed for long periods of time.

650-03 Reduce Cost-of-Living Adjustments in Social Security Benefits

	Outlay Savings (Millions of dollars)
2002	1,650
2003	4,000
2004	6,450
2005	8,850
2006	11,350
2002-2006	32,300
2002-2011	130,250

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

650-01 and 650-02

RELATED CBO PUBLICATION:

Long-Term Budgetary Pressures and Policy Options (Report), May 1998, Chapter 3.

Each year, the Social Security Administration adjusts monthly Social Security benefits by the increase in the consumer price index (CPI). For example, the 3.5 percent cost-of-living adjustment (COLA) effective for December 2000 was based on the increase in the CPI for urban wage earners and clerical workers (the CPI-W) between the third quarter of 1999 and the third quarter of 2000.

Some policymakers suggest that the law be changed to provide a COLA equal to the increase in the CPI minus a specified number of percentage points. The option presented here would limit the COLA to the increase in the CPI-W minus 0.5 percentage points, beginning with the COLA effective for December 2001.

This option would save $32.3 billion over the 2002-2006 period and more in later years. Because some Social Security beneficiaries with low income would qualify for federal means-tested benefits, such as Supplemental Security Income and food stamps, some of the savings in Social Security benefits might be offset by additional outlays for other programs. (That increase in outlays is not reflected in the estimates.)

Some analysts feel that the CPI overstates increases in the cost of living, but they debate the magnitude of the overstatement and what should be done about it. In 1996, the Advisory Commission to Study the Consumer Price Index (known as the Boskin Commission) estimated the size of the upward bias to be about 1 percentage point a year. If that is the case, then Social Security beneficiaries have been receiving increases in benefits beyond what is necessary to keep up with inflation. But that estimate is not universally accepted. Furthermore, since the commission prepared its report, the Bureau of Labor Statistics has changed the way it calculates the CPI to address several of the commission's concerns.

If the CPI has overstated increases in the cost of living for beneficiaries, then policymakers could reduce the COLA by a commensurate amount without lowering real (inflation-adjusted) benefits to beneficiaries below what they received when they became eligible for the program. Moreover, restricting cost-of-living adjustments in Social Security benefits could achieve considerable savings by exacting small reductions in benefits from a large number of people, in contrast with many other budget options that would impose large reductions in benefits on smaller groups.

The impact of even a small reduction in COLAs, however, would be quite large for future older beneficiaries whose benefits would reflect the cumulative effects of a series of smaller COLAs. The people whose benefits would be most affected would be the oldest beneficiaries and those who initially became eligible for Social Security on the basis of disability at an early age.

Moreover, whether or not the real value of the Social Security benefits received by older beneficiaries would then be below what it was when they first became eligible, their benefits would fall relative to those of new beneficiaries. That decline would occur because initial benefits would continue to be based on a formula in which past earnings are indexed to compensate for growth in nominal wages, which is the sum of inflation and real wage growth. Under current law, each new group of beneficiaries that begins receiving benefits at the normal retirement age receives a slightly higher average benefit than the group that became eligible the previous year, reflecting the increase in real wages. If policymakers reduced COLAs, the gap between consecutive age groups would widen accordingly.